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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

November 27, 2002

The Honorable Michael Powell
Chairman
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: Ex Parte Comments. In the Matter of Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers (CC Docket No. 01-338), Implementation of the Local Competition Provisions of the Telecommunications Act of 1996 (CC Docket No. 96-98), Deployment of Wireline Services Offering Advanced Telecommunications Capability (CC Docket No. 98-147)

Dear Chairman Powell:

As the Commission nears a decision in the Triennial Review of unbundling obligations of local exchange carriers, the Alliance for Public Technology (APT) would like to draw attention to the impact of these policies on consumers and the implications of these policies for universal, affordable access to advanced services and technologies. APT urges the Commission to reform the unbundled network element (UNE) pricing regime to ensure that it does not have a negative impact on advanced services and investment.

APT and the Consumer Interest

The Alliance for Public Technology (APT) is a nonprofit organization of public interest groups and individuals. APT's members work together to foster broad access to affordable, usable information and communications services and technology for the purpose of bringing better and more affordable health care to all citizens, expanding educational opportunities for lifelong learning, enabling people with disabilities to function in ways they otherwise could not, creating opportunities for jobs and economic advancement, making government more responsive to all citizens and simplifying access to communications technology. To this end, it is APT's goal to:

> make available as far as possible, to all people of the United States, regardless of race, color, national origin, income, residence in rural or urban area, or disability high capacity two-way communications networks capable of

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> enabling users to originate and receive affordable and accessible high quality voice, data, graphics, video and other types of telecommunications services.[1]

Remedies for Encouraging Robust Facilities Based Competition and Accelerating Deployment of Advanced Services

With ubiquity in deploying advanced networks as its primary objective, APT views creation of a workable competition model designed to accelerate investments in facilities by both incumbents and competitors to be a critically important step. Taking action to stimulate investments must deal with a new reality since the passage of the Telecommunications Act. The industry shows every sign of being a capital intensive, cyclical industry moving inexorably toward concentrations of market power with distinct possibilities of oligopoly becoming the "equilibrium" market structure.[2] The FCC must address the limitations of such competition in allocating telecommunications resources and focus more attention on monitoring investment and policies of all carriers.

The Triennial Review offers an opportunity for FCC to create a more stable environment, promote facilities based competition, encourage infrastructure investment and speed the transition to broadband technologies. The following suggested recommendations are tools to help achieve these goals.

- First, as market competition evolves, sunset requirements are needed for unbundling obligations imposed on ILECs. These should, however, include a transition period to minimize the impact.
- Second, the Act clearly permits forbearance when enforcement is unnecessary to insure just rates, consumer protection, or consistency with the public interest (i.e., when some sector is in the effective competitive zone, as is the case of ILEC provision of advanced services).
- Third, to ensure that these regulatory changes achieve the desired results, the Commission should establish a monitoring mechanism by which it can evaluate the impact of these changes on the welfare of consumers and ensure that regulatory objectives are aligned with consumer interests. **As** part of this process, the Commission should gauge the changes effects on both CLEC and ILEC investments.
- Fourth, exclude from unbundling 1) broadband networks and other new investments, including the high frequency portion of the local loop, packet switching, and fiber loop architectures; and 2) elements that competitors now provide in abundance over their own facilities, including circuit switching, dedicated transport, and high capacity loops. FCC jurisdiction over determination of which elements are subject to unbundling is crucial.

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[1] Alliance For Public Technology, *Principles to Implement the Goal of Advanced Universal Service* at *3* (1995).
[2] *How Telecom Is Becoming A Cyclical Industry, And What To Do About It* (DRAFT), Professor Eli Noam, Columbia University

- Fifth, require reporting and carefully monitor ILEC wholesale service quality to ensure competitors are not disadvantaged.

The Current Unbundling Regime is an Investment Barrier and Deterrent to Facilities Based Competition

The telecommunications sector and the economy as a whole are in a serious downturn. However, there is still no major facilities-based CLEC competition in the residential market, and there is a strong need for investment in today's and tomorrow's networks. Your own recent remarks highlight the enormous benefits of facilities based competition:

> *...Economic recovery means building business that can expand employment opportunities for our Nation's citizens. It means bringing real competitive choice to consumers and enhancing consumer welfare through differentiated products and services and differentiated pricing packages. It means, in short, investment in facilities. For only through facilities-based competition can an entity offer true product and pricing differentiation for consumers. Only through facilities-based competiiion will corporate spending on equipment thrive. Only through facilities-based competition can a competitor lessen its dependency on an intransigent incumbent, who if committed* io *frustrate entry has a thousand ways to do so in small, imperceptible ways. Only through facilities-based competition can an entity bypass the incumbent completely and force the incumbent to innovate to offset lost wholesale revenues. Only through facilities-based competition can our Nation attain greater network redundancies for security purposes and national emergencies.*[3]

Though some may advocate the UNE-P pricing model with the consumer interest in mind as a temporary measure to encourage competitors to enter the local phone market, in fact the current unbundling policies have had unintended consequences. UNE loops allow non-facilities-based telecommunications providers to deliver service without laying network infrastructure and, as a combination of UNEs, UNE-P allows end-to-end service delivery without provision of any facilities. While this model *does* assist competitors who might otherwise not be able to compete in the local market, when combined with the low TELRIC rates found in many states, UNE-P offers little incentive for these competitors to make the investment in their own facilities.

Based on future *optimal* network costs, TELRIC does not account for historical costs. Rather, it assumes carriers can rebuild their networks with the latest technology and highest efficiency. Even if carriers are not operating at optimal efficiency, under TELRIC, they are required to set their rates as if they were. The result is that UNE-P pricing based on the TELRIC method is often at a level so low that it does not allow the

3 Remarks of Michael K. Powell Chairman, Federal Communications Commission, at the Goldman Sachs Communicopia XI Conference, New York, NY, October 2,2002 [as prepared **for** delivery]

incumbent local exchange carriers (ILECs) to recover their own investment costs, thereby creating a disincentive for further investment by both the ILECs and their customers.

At the time TELRIC pricing was developed, the FCC reasoned that competitors needed access to the customer, and "resale" (in quotes to denote wholesale resale or UNE resale) gives them that crucial access; over time, they would build out their own modern networks as they would not wish to be dependent on the ILECs, and the ILECs would be forced to respond to this modernized competitor by in turn investing in advanced capabilities.

With little incentive to build out their own facilities, many CLECs are taking advantage of low cost network leases. In contrast, wireless and cable providers have built competing facilities without the benefit of UNE pricing. However, though facilities based competition is possible and alternative technologies are readily available, the number of UNE-P lines is steadily growing.

Long-term Consumer Interests Are Not Served by UNE-P

UNE-P is a temporary fix. It does provide easier entry, more apparent competition and lower prices *in the short-term.* However, focus on price alone is a shortsighted approach. While consumers need affordable rates, it should not mean further delay in access to the life-enhancing benefits of advanced services and technologies. Furthermore, UNE-P does not promote universal access. UNE-P providers are more likely to target lucrative business customers in the high profit urban areas with UNE-P networks, while neglecting the rural, underserved areas that would require greater facilities build-out to serve.

Some argue that competition alone will further investment by the incumbent carriers (e.g. in the form of network upgrades and buildout). To the contrary, this investment is more likely to be in CLEC-related services, such as back office electronic ordering and provisioning systems, not in new, innovative technologies or in network upgrades. With below cost UNE-P rates, this would be tantamount to the ILECs investing directly in their own competition. Competitive investments require a reasonable return on capital, measured against alternative investment options. Understandably, competitors are reluctant to invest in research and development, innovation and advanced services.

Telecommunications networks are capital intensive, and the financial community has no tolerance for investments without reasonable expectations of a competitive return. It is likely that the unbundling of broadband elements directly inhibits the growth of consumer access to high-speed Internet services.

Application of UNE-P to Advanced Services

Unbundling rules stand as a barrier to universal broadband deployment. Investment in advanced services is both capital intensive and financially risky and opening these new networks to competitors at below cost prices is a tremendous disincentive for investment. As AT&T's Chairman Armstrong said in reference to the then proposed AT&T – TCI merger, "No company will invest billions of dollars to become a facilities-based broadband services provider if competitors who have not invested a penny of capital nor taken an ounce of risk can come along and get a free ride on the investment and risk of others."[4] In that case, Chairman Kennard also supported the position that cable should not have to open up its broadband facilities, as this was a nascent technology that should not face such a burden. Clearly, this standard should also apply to the broadband services that are offered by the incumbent carriers.

We cannot possibly hope for facilities based competition in broadband if access to these very expensive systems is granted to competitors in one broadband platform, but not the others. The disparate regulations that govern the provision of broadband over cable modems and incumbent telephone facilities have created a market where cable is dominant and virtually unregulated. APT has called for technology neutral regulation of broadband services, and the Commission has an excellent opportunity to achieve a truly competitive market in broadband if the rules are balanced.

Section 706 of the Telecommunications Act of 1996 calls for deployment of advanced services to all Americans "in a reasonable and timely fashion." Continuation of current UNE-P rules does not advance the purposes of Section 706. The Commission is explicitly empowered by Section 706 to utilize methods that remove barriers to infrastructure investment. UNE-P is a primary barrier today; the regime in fact harms infrastructure investment, by creating false competition based on a resale model.

UNE-P, as it applies to local telephone service, is about creating consumer choices and opportunities for lower prices. With regard to advanced services, UNE-P rules contribute to the slow and uneven pace of deployment. For example, high-cost areas of the country are likely to remain without access because providers are unwilling to invest in unbundled networks where the return on investment is too low.

Furthermore, DSL and cable modems are merely transition technologies to the ultimate goal of ubiquitous access to the most advanced technologies and services. The implication of UNE-P for the long term could be to harm development of true two-way broadband to the home.

This is critical to consumers. Advanced services provide the opportunity to enhance the quality of life, particularly in traditionally underserved, high-cost areas. Consumers need access to broadband to tap the potential of applications, such as telemedicine, distance learning, public safety and many others. By exercising forbearance, the Commission can make it possible for millions of Americans to gain access to services that have the potential to improve the way they live, work and learn.

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[4] AT&T CEO Michael Armstrong, (CM, November 9,1998, p1.)

Jeopardizing Jobs, Growth and Prices

Without a fair return on investment, it becomes increasingly difficult to maintain current workforce levels. In the past **18** months alone, the communications and information technology industry has lost more than 500,000 jobs. As Morton Bahr, President of the Communications Workers of America has said, "[UNE-P] is bad public policy that can only exacerbate the meltdown of the telecom industry by creating even more job losses."'

By contrast, a regulatory environment that removes regulatory barriers and encourages investment can create new employment opportunities. According to a recent study, it is estimated that full broadband deployment would result in the creation of 1.2 million new jobs. Information technology jobs also pay, on average, **85%** more than other jobs.[6] Therefore, greater investment in a nationwide broadband network (from the release of UNE-P capital) could generate a significant number of high-quality jobs.

With unsustainable losses due to UNE-P', dominant carriers will look elsewhere for investments, hurting the economy and consumers. While the current regulatory framework eliminates the economies of scope and scale and discourages investment in more sophisticated networks, it also encourages investment in unregulated services in the U.S. and abroad. The downward trend in pricing prompts shareholders to shift their assets to competitors where the returns are greater, which could lead to higher rates. The wide variation in the setting of UNE-P rates by state regulators is also contributing to economic uncertainty and hindering investment, as uneven and inconsistent UNE-P application affects predictability as desired by both investors and consumers.

Creating a Competitive Future

Taken together, these implications indicate a need for regulatory reform. Changing UNE-P policies will help ensure that consumers benefit from the long-term security, reliability and growth of the public switched network and increased investment, innovation and access to advanced services. Encouraging true facilities based competition is the ultimate goal, both in the narrowband and broadband worlds. APT urges you and the FCC to seize this important opportunity to create a vibrant telecommunications future for all consumers.

Sincerely,

Matthew D. Bennett

Matthew D. Bennett
Policy Director

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5 Communication Workers of America October 15,2002 Press Release

6 *Putting Broadband on High Speed: New Public Policies to Encourage Rapid Deployment,* Stephen Pociask, Economic Policy Institute, July 2002

7 Merrill Lynch estimates that the four regional Bell companies will have **lost** an estimated $4.3 B of revenue by 2005– Telecommmunicator, September 23,2002.

Cc: Commissioner Kathleen Abernathy
Commissioner Jonathan Adelstein
Commissioner Michael Copps
Commissioner Kevin Martin